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C O N F I D E N T I A L SECTION 01 OF 03 MOSCOW 000056

SIPDIS

DEPT FOR EUR/RUS, EEB/ESC/IEC GALLOGLY AND GREENSTEIN,  
S/EEE MORNINGSTAR  
DOE FOR HEGBURG, EKIMOFF  
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E.O. 12958: DECL: 01/12/2020  
TAGS: [EPET](#) [ENRG](#) [ECON](#) [PREL](#) [RS](#) [KGHG](#)  
SUBJECT: RUSSIA STRIVES TO REDUCE GAS FLARING

REF: 08 MOSCOW 3321

Classified By: EconMinCouns Matthias J. Mitman, Reasons 1.4 (b,d)

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SUMMARY  
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11. (C) Russia flares more natural gas than any other country, burning over 40 bcm in 2008. The GOR plans to reduce this figure by raising Russia's associated gas utilization level to 95% by 2012 from the current 60-70% rate. Experts doubt, however, that the GOR will achieve this goal. Obstacles include an inability to measure utilization, a shortage of gas processing and transportation infrastructure, the short time-frame of the target, and the lack of third-party access to gas and electricity grids. That said, the Duma and several GOR agencies are developing legislation and regulations targeting the access issue, and Russia's top oil companies have already announced plans to meet the target. In addition to an effective GOR system to impose fines on companies who fail to comply with flaring regulations, successful achievement of the GOR's goal will require a resolution of the access issue and incentives for investment in utilization technologies. End Summary.

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GOR GETS SERIOUS ABOUT GAS FLARING  
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12. (SBU) According to satellite data collected by the U.S. National Oceanic and Atmospheric Administration, Russia is the world's worst offender in terms of natural gas flaring, which along with venting represents a major source of greenhouse gas emissions. (Note: Flaring or burning occurs to dispose of associated natural gas liberated during crude oil production and processing, most often in remote areas where there is no gas transportation infrastructure or local gas market. End Note.) In 2008, Russia flared 40.2 bcm, almost 10 bcm less than the previous year, but still 25 bcm more than second-place Nigeria. By comparison, Turkey consumed only 37 bcm of gas in 2008. Despite satellite data to the contrary, the GOR officially reports that Russia flares only 20 bcm of gas per year. According to a 2008 World Bank (WB) study, it could be economically viable to use up to 80% of Russian gas currently flared, generating several billion dollars per year and eliminating millions of tons of carbon dioxide emissions.

13. (SBU) The GOR plans to reduce flaring by increasing Russia's associated gas utilization level to 95% by 2012. The Ministry of Economic Development estimates that the average oil company in Russia currently uses only 60-70% of associated gas. In a November 2009 speech to the Federation Council, President Medvedev said that flaring was one of the most ineffective uses of energy resources, underscoring that it "pollutes the environment and sends tens of billions of rubles up in smoke." Prime Minister Putin warned oil company executives in November 2009 that the GOR was serious about its target for reducing gas flaring and would levy huge fines against companies failing to comply.

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THE STEEP ROAD FROM 60 TO 95 PERCENT  
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14. (C) Anastasiya Rozhkova of the WB's Oil, Gas, Mining, and Chemicals Department told us the GOR faced considerable obstacles to meeting its 2012 target in terms of data, infrastructure, timing, and market barriers. First and foremost, Rozhkova stated the GOR lacks accurate measurement and reporting mechanisms to track how much gas companies flare and where they do so, in order to identify appropriate solutions and assess their utilization plans. Many companies flare gas because their oil fields are located in remote locations without access to transportation or processing infrastructure. Rozhkova noted that the 2012 deadline does not provide sufficient time to complete the types of projects required to reach the 95% target, even if companies already had plans and financing. Finally, those companies with

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fields close to gas pipelines and electrical grids (into which they could sell associated gas-generated electricity) often find themselves unable to sell their gas or electricity because state-owned monopolies controlling the systems refuse to buy. (Note: The Federal Network Company of the Unified Energy System (FSK) controls access to Russia's electrical grid and determines which electricity producers will be used to meet network demand at any given time. End Note.)

15. (C) The lack of adequate third-party access (reftel) to Gazprom's network has sparked several disputes with oil companies, even with other state-owned corporations. Gazprom controls the country's internal gas transportation network and is by law the only company that can export gas. Rosneft has taken Gazprom to court in the past over lack of access to its network. Rozhkova told us that Gazprom agreed to take gas from Rosneft as a result of the case, but when the time came to make the purchase, Gazprom refused to do so, claiming that it already had enough gas. Rosneft is now suing Gazprom for the amount of the environmental fines levied against it for flaring the gas it was unable to sell. The Federal Anti-Monopoly Service (FAS) is also considering a Rosneft case against Gazprom over third-party access to the gas network. FAS and the Federation Council Natural Monopoly Committee are both developing draft laws to address gas utilization access and utilization issues. (Note: EPA's Methane to Markets program is working with Gazprom and other Russian actors to identify ways to reduce Russia's greenhouse gas emissions. End Note)

16. (C) In November 2009, Prime Minister Putin announced that gas-powered electricity plants using associated gas would receive priority access to Russia's electrical grid as an incentive for capturing gas instead of flaring it. The Duma is also taking steps to address the flaring issue, having passed in June 2009 the first reading of a draft amendment to the electricity law that mentioned production from associated gas. However, Rozhkova doubts the amendment under Duma consideration will resolve the problem of access to the grid, which is controlled by FSK, because it fails to give associated gas priority over non-associated gas as a source of electricity and does not include clear measures to help oil companies sell electricity. Furthermore, she said, the

draft law does not address the issue of how regions that are already producing their electricity from associated gas could export new production to other areas.

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LUKOIL AND TNK-BP PLAN TO FINISH ON TIME  
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17. (C) Russia's top three oil companies -- Rosneft, LUKoil, and TNK-BP -- have already announced plans to reduce gas flaring in an effort to meet the target rate for gas utilization. In December 2009, Steve Allen, LUKoil Head of Investor Relations, told us his company was not concerned about meeting the 95% target because it already used 91% of its associated gas. Despite difficulties encountered by Rosneft in its attempts, LUKoil has been successful in selling most of its associated gas to Gazprom. Allen did note that while Gazprom was a good negotiating partner, it often purchased LUKoil's gas for less than the European market price. In addition, LUKoil is planning an associated gas-powered electricity plant in the Caspian region.

18. (SBU) In 2006, TNK-BP announced its intention to reduce flaring to no more than 5% of total gas production by 2010, with further reductions in the future. Company executives planned over \$500 million in associated gas projects, including a joint venture with Sibur in Nizhnevartovsk to resolve gas processing capacity constraints and an expansion of its gas processing capacity in Orenburg. TNK-BP anticipates a comprehensive associated gas handling solution will complement every oil field development project.

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COMMENT  
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19. (C) GOR prioritization of flaring reduction and

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significant investments by Russia's major oil companies in associated gas utilization are positive steps in addressing the problem. The GOR's current emphasis on punitive fines, however, may not prove to be enough. Successful achievement of its goal will also require regulatory reform, and enforcement, to ensure third party access to Russia's gas and electricity grids as well as incentives to encourage investment in new technologies that increase associated gas utilization. End Comment.  
Rubin